Nos. 21,607 and 21,607-A

United States Court of Appeals

For the Ninth Circuit

D. Clifford Crummey and
Ethel Elizabeth Crummey,
Petitioners,
vs.
Commissioner of Internal Revenue,
Respondent.

On Petition to Review Decisions of the Tax Court of the United States

REPLY BRIEF FOR PETITIONERS

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PRELIMINARY STATEMENT

Petitioner filed his brief in his petition for review on June 23, 1967, and the brief for Respondent was received by Petitioner's attorney on July 25, 1967. This Reply Brief is therefore due to be filed on or before August 24, 1967.

ARGUMENT

In his brief, the Commissioner reasons that the gifts in trust for the minor beneficiaries fail to qual-

ify for the annual exclusion essentially for two reasons.

First, local law precludes a minor from demanding distribution from the Trustee because of his non-age.

We submit that the statutory provisions cited in the opinion of the Court below, in the taxpayers' brief and again the Commissioner's Brief were enacted to protect minors from unfortunate commercial transactions entered into because of their inexperience. We submit further than an objective analysis of the California law discloses that a minor has no lack of capacity to accept a gift and that such capacity is not terminated merely because the minor must ask or demand to receive such gift.

And Second, that even if California law permitted such demand, the Trustors here intended that the right to demand not be exercised.

These are, in general, the same arguments urged by the Commissioner in each of the cases raising the issue of the tax effect of a trust which provides for the minor's right to demand distributions. The *demand* clause in the Crummey trust did not specify nor in any manner evidence the trustor's intent to be that the beneficiaries must make their demand *subsequent* to a transfer in any year. Certainly, a valid, effective demand could be made upon the trustee on January 1 requiring distribution from transfers made later in the year. This is recognized by the Commissioner who allowed without question, the present interest nature and related exclusions relating to

transfers for the beneficiaries over age twenty-one. His disallowance of the exclusion of identical transfers for the minor beneficiaries only serves to dramatize his inconsistency and the inequities inherent in his administration of this gift tax provision, reversed in the many cases cited below

There is another inconsistency also; as noted in the reproduction of the *demand* clause (Br. 4), the trust provided ". . . the child's guardian *may* make such demand. . . ." After faithfully reproducing the clause the effect of which is before the Court in this case, the Commissioner repeatedly insists that the trust provides that such a demand *could only be made through a guardian.* This patent misconstruction is repeated on almost every page of the Commissioner's brief. The use of "may" has always been permissive, was accurately construed in this manner by the Court below, and this misleading construction given thereto by the Commissioner serves only to becloud the issue before the Court.

The leading case in this area is *Trust No. 3 v. Commissioner,* 285 F.2d 102. The *demand* clause before the Seventh Circuit in this 1960 case, and the Court's well reasoned analysis favoring the taxpayer follow. The *demand* clause:

> The beneficiaries shall be entitled to all or any part of their share of the trust or to terminate the trust estate in whole or in part at anytime whenever the said Sylvia Brehm, Karen Brehm and Jane Elizabeth Brehm or the legally appointed guardian for one of their estates shall

make due demand thereof by instrument in writing, filed with the then Trustee and, upon such demand being received by the Trustee, the Trustee shall pay said trust estate and its accumulations or the part thereof for which demand is made over to said beneficiaries or to the legally appointed guardian for any one of their estates who made such demands on their behalf.

The Court's analysis:

During the period from March 4, 1954, to December 31, 1956, the beneficiaries under the trust indenture were under the age of twenty-one years. Moreover, they had no legally appointed guardian during that period.

* * * *

In his brief in this court the Commissioner brings our problem into focus by stating:

> "The germane inquiry here is whether there could have been an actual termination of the trust or the taking of any part of the trust corpus or income on behalf of these beneficiaries during either of the taxable years before this Court."

He proceeds to answer his own inquiry by asserting that under the trust indenture only the beneficiaries or their legally appointed guardians could terminate the trust estate and that, inasmuch as the beneficiaries were minors during the years in question, they could not themselves terminate the trust, and, there being no guardian appointed during those years, there was then "no one who was immediately qualified to make

the prescribed demand set forth in Paragraph V."

* * * *

We believe that, for several reasons, the Commissioner's argument lacks substance. It is not denied by him that the beneficiaries were given a right to terminate the trust and to take possession of the trust property, but he considers that their minority bars them because (he says) they could not assert that right except through a guardian duly appointed. This distinction is unconvincing in view of the fact that the appointment of a guardian for a minor under a state law is a matter of routine in which the federal government has no concern. To effectuate a termination of the trust as to any child and a delivery of its share of the accumulated income or corpus to the child, customarily there would be delivered to the Trustees a properly authenticated copy of letters of guardianship and a receipt for the assets and monies delivered. However, we think the necessity of such routine steps would have no bearing upon the fundamental question of the legal right of the beneficiaries to terminate the trust. *We should not deny an undisputed right because the conventional methods of exercising it have not been described in the instrument creating the right.* (Emphasis added.)

An even later decision, *Griffith v. United States,* U.S. District Court, S. Dist. Texas, Houston Div., Civil Action No. 13,414, 12/13/62; 63-1 USTC Para. 12, 124; 11 AFTR 2d 1785 cites numerous cases in this field which reject the Commissioner's overly technical viewpoint:

The *demand* clause (in part):

> "The trust herein created and all gifts to the trustees hereunder shall be irrevocable so far as the trustees and trustors are concerned, but said trust may be terminated at any time upon demand of the beneficiary, if legally capable of acting for himself, or of any duly appointed and qualified guardian of his estate having the power to manage and control the same."

* * * *

The Court's analysis:

> Under Section 2503(b) the exclusion may not apply where the gift is a future interest in property. The guiding principles on the subject were set forth in the leading case of *Fondren v. Commissioner of Internal Revenue,* 324 U.S. 18, decided January 29, 1945. Accord: *Commissioner of Internal Revenue v. Disston,* 325 U.S. 442, decided June 4, 1945.
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> * * * *
>
> The taxpayer claiming the exclusion must assume the burden of showing that the value of what he claims is other than a future interest. Cf. *New Colonial Co. v. Helvering,* 292 U.S. 435. *Commissioner of Internal Revenue v. Disston,* supra, at page 449. That burden has been fully satisfied in this case.
>
> It is evident the subject trust instruments were intended to satisfy the test for present interest established in the *Fondren* case. I find that the trust instruments purported to, and did in fact, create a right to a present interest in property in the minor beneficiaries. The gifts made

> to and under the trusts were of a present interest. *It is abundantly clear that the statutory exclusion was not intended to discriminate against minors.* *Fondren v. Commissioner of Internal Revenue,* supra at pages 28, 29; Title 26, U.S.C.A. Section 2503(c). The possible need of legal guardianship does not itself defeat the present interest nature of the donation. *Kieckhefer v. Commissioner of Internal Revenue,* 7 Cir., 189 F.2d 118; *Gilmore v. Commissioner of Internal Revenue,* 6 Cir., 213 F.2d 520; *Trust No. 3 v. Commissioner of Internal Revenue,* 7 Cir., 285 F.2d 102; *United States v. Baker,* 4 Cir., 236 F.2d 317; *Commissioner of Internal Revenue v. Sharp,* 9 Cir., 153 F.2d 163 Contra: *Steifel v. Commissioner of Internal Revenue,* 2 Cir., 197 F.2d 107, decided May 15, 1952. (Emphasis added.)

The *Trust No. 3* and *Griffith* decisions articulate well the present state of the law in this area. Another recent case, *Ross v. United States,* 348 F.2d 577, decided with reference to section 2503(c), nevertheless provides a succinct review of the problem area:

> That state laws pertaining to guardianships might pose barriers to the immediate enjoyment of a gift in trust will not cause the gift to be denied present interest status. *Baker v. U.S.,* 4 Cir. 1956 236 F.2d 317 (50 AFTR 1). See also *Strekalovsky v. Delaney,* D. Mass. 1948, 78 F. Supp. 556 (37 AFTR 96); *Cannon v. Robertson,* W.D.N.C. 1951, 98 F.Supp. 331 (40 AFTR 1079); 5 Mertens Law of Federal Gift and Estate Taxation Section 38.12 at 499; Lowndes & Kramer Federal State and Gift Taxes Sec. 33.12 at 728; 2 Casner, Estate Planning 255. The district court

> in Arizona has held that a gift to minors in trust qualified for the annual exclusion even though "resort to a court of equity might be necessary" in order for the trustee to invade the trust principal. *DeConcini v. Wood,* D.C. Ariz. 1960, 1 U.S.T.C. par. 11,938, 5 AFTR 2d 1874.
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> * * * *
>
> The future interest exception, adopted in 1932, was a legislative response to the specific administrative difficulty, in some cases, "of determining the number of eventual donees and the values of their respective gifts." H. Rep. No. 708, 72d Cong., 1st Sess. 29 (1932); S. Rep. No. 665, 72d Cong., 1st Sess. 41 (1932). The courts perhaps because the language of the statute was so broad, extended the future interest concept beyond the limits to which Congress, later, was willing to go. . . .

From this it can be seen that the position tendered by the Commissioner is a highly technical one supported in one Appellate decision, *Steifel v. Commissioner,* 197 F.2d 102 (Br. 11, 15, 17, 18, 20) but discredited as unrealistic, and unfair to minor donees in one case after another since the 1945 *Steifel* decision. The landmark Supreme Court decision, *Fondren* also cited often in the Commissioner's brief is actually neutral as authority in these cases. It announces the "tax" definition of a future interest, which differs somewhat from the "common law, real property" definition, but leaves to the Courts the application of its definition to specific cases. *Fondren,* although cited and followed in *Steifel,* has been cited and followed

in most of the cases which adopt the more realistic position of permitting the annual exclusion.

In an early case, this Court rejected the restrictive interpretation sought by the Commissioner and permitted the gift tax exclusion for transfers into trust where the trust instrument gave the trustee discretionary authority to pay income to the mother or the guardian of the minor beneficiaries, *Commissioner v. Sharp* (C.A. 9 1946, 153 F.2d 163). Similarly, in *U.S. v. Baker,* 236 F.2d 317, where the taxpayers made trust transfers for their minor grandchildren giving the trustee broad powers similar to those of a guardian, the Court held that the minor grandchildren acquired present interests qualifying for gift tax exclusions. Also, in *Albright v. United States,* 308 F.2d 739, where the Fifth Circuit, though not analyzing a *demand* clause, refused to apply a statutory provision designed to resolve an "administrative difficulty" in such a manner to treat a trust transfer for minor beneficiaries as a future interest. In that case the Court resolved a drafting ambiguity so as to support the gift tax exclusion. Similarly in *Strekalovsky v. Delaney,* 78 F.Supp. 556, where the trust "provided that upon the demand of any legally appointed guardian of any of the children, the entire share was to be paid to said guardian", the Court citing this Court's decision in *Sharp,* found a sufficient present interest in the minor beneficiary to support the gift tax exclusion even though no guardian had, in fact, been appointed. Also, following *Sharp, Strekalovsky* and *Kieckhefer,* was the Court in *Cannon v.*

Robertson, 98 F.Supp. 331, which allowed the gift tax exclusion, reasoning:

> Commissioner of Internal Revenue v. Sharp . . . is a very interesting case and throws a considerable amount of light on the thinking of the court in matters involving a like controversy. Judge Garrecht's reasoning is all embracing and his decision fortifies the law in matters of this kind.
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> * * * *
>
> The most recent case is that of Kieckhefer . . . and on facts almost wholly similar to the facts embraced herein, and in which it was decided that the gift was one of a present rather than a future interest.

SUMMARY OF ARGUMENT

The taxpayer agrees with the Commissioner that the trust transfer is not unlike the transfer in *Steifel;* we submit that the transfers in *Trust No. 3, Griffith, Kieckhefer, Gilmore, Perkins,* and other cases are likewise not dissimilar. We ask this Court to follow its decision and often-cited reasoning in *Sharp,* to once again reject the restrictive and highly technical construction urged by the Commissioner, to avoid discriminating against trust transfers for the benefit of minor beneficiaries, and to recognize the existence of the present interest and qualification for the gift tax exclusion.

Dated, Sacramento, California,
August 18, 1967.

Respectfully submitted,
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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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